

Message Text

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ACTION EA-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-03
INR-10 NSAE-00 ICA-11 TRSE-00 XMB-02 OPIC-03
SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-07
CEA-01 L-03 H-01 PA-01 DOE-15 SOE-02 AGRE-00
ITC-01 CTME-00 /114 W
-----084867 031152Z /15

R 031123Z APR 78
FM AMEMBASSY TOKYO
TO SECSTATE WASHDC 6734

C O N F I D E N T I A L SECTION 01 OF 02 TOKYO 05536

E.O. 11652: GDS
TAGS: OVIP (FUKUDA, TAKEO)
SUBJECT: FUKUDA VISIT PAPER: STATE OF JAPAN'S DOMESTIC
ECONOMY

1. THE JAPANESE GOVT HAS SET AS ITS OBJECTIVE FOR
DOMESTIC GROWTH IN FY 78 A TARGET OF 7 PCT REAL GROWTH.
ITS OBJECTIVE IS TO ACHIEVE THIS TARGET WHILE AT THE SAME
TIME DECREASING THE CURRENT EXTERNAL SURPLUS, OR IN OTHER
WORDS, MODIFYING JAPAN'S RELIANCE ON EXPORT-LED GROWTH.

2. MOST OBSERVERS BELIEVE THAT GROWTH IN THE YEAR AHEAD
IS APT TO FALL SHORT OF THE 7 PCT RATE -- WITH THE LIKELY
OUTCOME USUALLY PUT SOMEWHERE BETWEEN A 4 1/2 AND 6 PCT
RATE. THERE IS NEVERTHELESS CONFIDENCE AND A BROAD CON-
SENSUS THAT THERE WILL BE SUBSTANTIAL GROWTH, WHETHER OR
NOT THE 7 PCT TARGET IS HIT ON THE NOSE. WE BELIEVE THAT
THIS CONFIDENCE IS WELL FOUNDED, FOR SEVERAL REASONS.
ONE IS THAT THE PAST TWO CALENDAR YEARS SAW REAL GROWTH OF
6 PCT AND 5 PCT RESPECTIVELY. THE SECOND IS THAT IMBAL-
ANCES IN THE DOMESTIC ECONOMY ARE BEING REDUCED, NOT
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AUGMENTED. FINALLY, MORE RAPID THAN ANTICIPATED PROGRESS
IN REDUCING INFLATION (THE INCREASE IN CONSUMER PRICES
THIS YEAR MAY BE DOWN TO ABOUT 5 PCT) BODES WELL FOR
FUTURE LEVELS OF ECONOMIC ACTIVITY.

3. STRONG GROWTH IN THE FIRST HALF OF CALENDAR YEAR 77 WAS
FOLLOWED BY A PAUSE IN THE THIRD QUARTER AND A MODERATE

(AT ABOUT A 4 PCT SEASONALLY ADJUSTED ANNUAL RATE) RECOVERY IN THE FOURTH QUARTER. A FAIRLY STRONG RECOVERY OF INDUSTRIAL PRODUCTION BEGAN LAST NOV, AND CONTINUED THROUGH JAN. ALTHOUGH INDUSTRIAL PRODUCTION SPUTTERED IN FEB, THE STRONG UPTURN IN THE PREVIOUS THREE MONTHS REPRESENTED WELCOME EVIDENCE OF LIFE IN THE KEY INDUSTRIAL SECTOR.

4. WE BELIEVE THAT JAPAN COULD IN FACT ACHIEVE ITS 7 PCT GROWTH TARGET IF THINGS BROKE RIGHT. ONE OF THE

MOST CRITICAL PROBLEMS, ALONG WITH REACTION TO YEN APPRECIATION, IS THE REACTION OF CONSUMERS AND BUSINESSMEN TO THE HEAVY DOSE OF FISCAL STIMULUS IN THE FY 78 BUDGET. GIVEN JAPAN'S RELATIVELY SMALL CENTRAL GOVT SECTOR, THE SUCCESS OF FISCAL POLICIES DEPENDS EVEN MORE IN JAPAN THAN IN OTHER COUNTRIES ON THE REACTION OF THE PRIVATE SECTOR (AND LESS ON THE DIRECT EFFECTS). IN THE PAST, HOWEVER, THE GOVT, AS WELL AS THE PUBLIC, HAS TENDED TO REACT TO UNCERTAINTIES AND EVEN TO MANAGEABLE PROBLEMS (INCLUDING THE SUBSTANTIAL APPRECIATION OF THE YEN) WITH A CRESCENDO OF HANDWRINGING; NOW, HOWEVER, IT IS EVIDENT THAT THE GOVT IS UNDERTAKING A FAIRLY WELL-CONCERTED EFFORT AT CONFIDENCE BUILDING. IT IS TOO SOON TO JUDGE THE SUCCESS OF THESE EFFORTS, BUT THEY ARE CERTAINLY TO BE APPLAUDED AND SUPPORTED.

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5. THE PRIME MINISTER IS HEAVILY COMMITTED POLITICALLY TO ACHIEVING STRONG ECONOMIC GROWTH. IN PART THIS IS BECAUSE HIS POLITICAL REPUTATION DEPENDS MOSTLY ON WHETHER HIS PERFORMANCE MATCHES HIS REPUTATION AS AN ECONOMIC WIZARD. IN PART, IT IS BECAUSE HIS POLITICAL ADVERSARIES, BOTH WITHIN THE LDP AND IN OTHER PARTIES, HAVE ACTIVELY AND SUCCESSFULLY SOUGHT TO COMMIT HIM AS DEEPLY AS POSSIBLE TO THE 7 PCT TARGET (ALTHOUGH RECENT YEN APPRECIATION HAS WEAKENED HIS OPPONENTS' CASE). THE PROSPECTS FOR ACHIEVING THE TARGET WILL BE MUCH CLEARER BY THE TIME OF THE LDP PRESIDENTIAL ELECTION NEXT DEC. RENEWED YEN APPRECIATION HAS TEMPTED SOME IN THE GOVT TO ATTEMPT TO GET OUT FROM UNDER THE TARGET, BUT FUKUDA HAS THUS FAR RESISTED THAT TEMPTATION. WE BELIEVE HE WILL CONTINUE TO DO SO, AS LONG AS POSSIBLE, ABSENT A FURTHER DRAMATIC CHANGE IN CIRCUMSTANCES.

6. IT IS TO BE BORNE IN MIND THAT THERE HAS BEEN CONSIDERABLE CONTROVERSY HERE AS TO WHETHER THE 7 PCT TARGET WAS ESTABLISHED AS A RESULT OF DOMESTIC DECISIONS OR PRESSED UPON THE JAPANESE BY THE U.S. WHILE CONCEDING INTERNATIONAL INTEREST, FUKUDA HAS TAKEN THE POSITION

PUBLICLY THAT THE COMMITMENT IS A DOMESTIC ONE.

7. IT MAY BE ASSUMED THAT FUKUDA WILL INTRODUCE ADDITIONAL FISCAL STIMULUS SHOULD HE BELIEVE THAT ACHIEVEMENT OF THE 7 PCT TARGET IS ENDANGERED. OFTEN CRITICIZED FOR BEING SLOW IN REACTING TO CHANGED ECONOMIC CIRCUMSTANCES, HE MAY OPT FOR HASTE THIS TIME AROUND. HE HAS ALREADY GONE ABOUT AS FAR AS COULD BE EXPECTED AT THIS STAGE IN SUGGESTING THAT A SUPPLEMENTARY BUDGET WILL BE INTRODUCED IF NECESSARY. THE OFFICIAL DISCOUNT RATE WAS REDUCED TO A POSTWAR LOW OF 3 1/2 PCT ON MARCH 16.

8. IT WOULD BE USEFUL FOR US:

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ACTION EA-12

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R 031123Z APR 78
FM AMEMBASSY TOKYO
TO SECSTATE WASHDC 6735

C O N F I D E N T I A L SECTION 02 OF 02 TOKYO 05536

--TO REAFFIRM THE FUNDAMENTAL IMPORTANCE WE ATTACH TO STRONG, NON-INFLATIONARY GROWTH ON THE PART OF JAPAN AS A KEY ELEMENT IN SECURING WORLD ECONOMIC RECOVERY.

--TO EXPRESS APPRECIATION FOR THE SETTING OF AN AMBITIOUS GROWTH TARGET, DESPITE THE POLITICAL RISKS INVOLVED.

--TO STATE CLEARLY THAT WHILE WE WELCOME JAPAN'S CON-

TINUED COMMITMENT TO THIS 7 PCT TARGET, FOR OUR PART WE
UNDERSTAND THAT IN THE FINAL ANALYSIS ECONOMIES CANNOT BE
MANAGED WITH PINPOINT ACCURACY. MANSFIELD

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